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SUBJECT: ABU DHABI CAUTIOUSLY POSITIVE ON SWF BEST PRACTICES

REF: ABU DHABI 1294

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11. (SBU) Summary: Abu Dhabi financial officials told a Treasury delegation, led by DAS Ahmed Saeed that they welcomed the opportunity to cooperate with the USG. ADIA Managing Director Sheikh Ahmed bin Zayed Al-Nahyan and Yousef Al-Otaiba, Foreign Affairs Director for Abu Dhabi Crown Prince Sheikh Mohammed bin Zayed Al-Nahyan responded positively to Treasury's proposal for voluntary best practices for Sovereign Wealth Funds and expressed interest in further details. Officials all stressed ADIA's role as a long term passive investor and that the new Abu Dhabi Investment Council (ADIC) would take the same position. End Summary

12. (SBU) On September 19, a delegation led by Ahmed Saeed, Treasury DAS for Middle East and Africa, including Robert Kaproth, Director of Treasury's Office of International Monetary Policy visited Abu Dhabi to explain Treasury's proposal for Sovereign Wealth Funds (SWFs) and investment recipient countries to work together under an IMF/WB umbrella to create voluntary best practices for SWFs. They met with Sheikh Ahmed bin Zayed Al-Nahyan, Managing Director of the Abu Dhabi Investment Authority (ADIA); Hamad Hurr Al-Suwaidi, Under Secretary Abu Dhabi Department of Finance (and ADIA board member); Jean Paul Villain, Chief Investment Advisor ADIA; Khalifa Al-Kindi, Managing Director Abu Dhabi Investment Council (ADIC); and Yousef Al-Otaiba, Foreign Affairs Director for Abu Dhabi Crown Prince Sheikh Mohammed bin Zayed Al-Nahyan.

13. (SBU) Saeed and Kaproth stressed the U.S. commitment to an open investment climate. They noted that well-run SWFs such as ADIA have had a positive impact on international financial stability as long-term investors without leverage. The growth in both the size and the number of SWFs, however, represented a structural shift in the international financial system that needed to be better understood. In addition, the increased attention to these SWFs could lead to increased financial protectionism. The proposal to develop voluntary best practices, jointly, would address concerns about these proliferating SWFs and would serve as a tool to resist protectionist sentiments in recipient countries. In parallel, Treasury was suggesting that the OECD work together to create a voluntary code of best practices for recipient countries.

14. (SBU) Best practices would cover areas such as fund objectives, operational and risk management, governance structure, accountability, and transparency. In addition, they would ensure that SWF investment criteria were commercial/financial rather than foreign policy driven. Public statements from ADIA, as a passive portfolio investor, that its decisions are made on a strictly commercial basis would help allay public concerns. Best practices would not deal with an SWF's asset allocation decisions. Different SWFs had different philosophies, and appetite for risk and investment decisions should remain a decision for the SWF and its government.

ADIA Value Cooperation -- Avoid Public Exposure

15. (SBU) Saeed explained that the US Treasury views ADIA as a valuable member of the international financial system. SWFs were proliferating, however, and the size of assets under management was increasing to trillions of dollars, which raised a very real risk of protectionist backlash. He said Treasury had sent delegations to Asia, Europe, and now the Middle East. He stressed that he thought ADIA was already doing much of what might be considered best practices. Sheikh Ahmed said ADIA officials had become aware of growing fears and protectionist sentiment with regard to SWFs. He stressed that he had no problem dealing with other governments and assured Saeed that ADIA was willing to cooperate with the U.S. to look for solutions. He stressed, however, that ADIA did not want to either raise its public profile or talk to the media. Saeed probed saying he sensed ADIA supported the concept of guidelines, mutually agreed on in coordination with the IMF/WB, but wanted to be sure that he was correct in his understanding. Sheikh Ahmed responded that it would be no problem, that he was ready to cooperate on the proposal, and that he would be interested in learning

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more about it after Ramadan.

16. (SBU) Sheikh Ahmed explained that ADIA has always been a conservative organization, whose first aim is to protect and maintain the assets of the Emirate of Abu Dhabi. ADIA's second goal, he noted, was to increase the size of these assets. Sheikh Ahmed asked whether the delegation had seen other SWFs. Kaproth explained that he had made two trips to Asia and Europe and that Treasury had separate contacts with China. In response to Sheikh Ahmed's question, Kaproth noted that China was very interested in minimizing financial protectionism issues. More broadly, he added, there was strong interest in Asia in IMF/WB guidelines. He had the impression that some of the older SWFs were concerned that the rise of new funds raised reputational risks. He explained that in Europe, Norway came to the G-20 meeting at Treasury's invitation to show how it managed its funds. Saeed explained that the proposal for voluntary best practices would serve as a benchmark to help ADIA and other well-run SWFs distinguish themselves from some of the newer SWFs, which were not so well-run.

Abu Dhabi Investment Council -- "We just want to make money"

17. (SBU) Khalifa Al-Kindi stressed that both ADIA (where he previously served as Deputy Managing Director) and ADIC were passive investors. ADIA had decided "a long time ago" not to buy a stake in any one company larger than the relevant regulator's disclosure limit (normally never more than four percent). He also asserted neither ADIA nor ADIC would push hostile takeovers of companies. It would pose "a problem for us," he stated. ADIA's overall objective, he explained, was to beat the average OECD inflation rate by about five to six percent. He noted that the strategy and allocations had developed over the last 17 years. The major difference between ADIA and ADIC, he said, was that ADIA had liabilities

to the government of Abu Dhabi. (Note: ADIA manages the bulk of the Emirate of Abu Dhabi's external assets and serves as the Emirate of Abu Dhabi's "check book" or supplementary source of financing. End Note.) The government has told ADIC that it would have no liability to the government, which would allow it to invest in more illiquid assets.

¶8. (SBU) Al-Kindi asked what the concern was about SWF, noting that "I assume our custodians are disclosing" investments to relevant regulators. Kaproth explained that the growth in the size and number of these funds was drawing attention. Al-Kindi asserted that the entire GCC foreign asset holdings were "small beans" compared to China's. Kaproth replied that oil exporters' foreign assets roughly matched Asia's. Al-Kindi also questioned the public perception of ADIA's size, stating "\$750 billion is way too big" and that he annually gave the IMF figures on the size of ADIA. He stressed, however, that ADIA -- as a matter of policy -- did not disclose the size of its foreign investments publicly. Confidentiality, he noted, was a policy directed "from above."

¶9. (SBU) Looking forward, Khalifa noted that he was seeing asset price inflation and shrinking expected returns in traditional asset classes. Investors would need to diversify their investments. In response to the question of whether he worried about the increasing rhetoric surrounding SWFs, Khalifa said no, but acknowledged a need to be careful. He stressed that neither ADIA nor ADIC wanted conflict with the countries in which it invested. For that reason, he stressed, neither company took large stakes in companies.

¶8. (SBU) Al-Kindi stated that all local banks in Abu Dhabi were exposed to sub prime mortgage backed securities. The funding costs to the region had increased dramatically already. In order to meet the development plans of the region, the banks were relying on medium term notes to fund this expansion, a market which, he noted, was now largely closed. He said that he foresaw bank profitability suffering and a drop in returns for investors. In the case of Dubai, he stated that Dubai was highly leveraged and "buying equities with borrowed cash."

Crown Prince's Office -- Concerned about Protectionism

¶9. (SBU) Al-Otaiba opened the meeting with Saeed by noting that some in the UAE were a bit paranoid after DP World and

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asking whether these new SWF proposals targeted the UAE or everyone. Saeed replied that these guidelines would be developed for all SWFs and would be developed in concert with investor nations and nations receiving investment. He stressed that the Administration remained committed to maintaining an open investment climate and wanted to prevent future problems. The growth of SWFs to trillions of dollars increased attention and the risk of a protectionist backlash from some countries. He noted that the UAE would be announcing two high-profile investments in the upcoming week. (Note: The Dubai Bourse-NASDAQ deal and Mubadala's purchase of a non-voting stake in the private equity firm Carlyle. End Note.)

¶10. (SBU) Al-Otaiba asked whether the various SWFs would sign up to creating these voluntary best practices, noting that consensus-building among funds with widely different investing styles would be difficult. Kaproth noted that best practices already existed for fiscal and monetary policy and for reserve management. Kaproth noted that working with the IMF and the World Bank also allowed both commodity and other SWFs to participate. Al-Otaiba said his view was that ADIA was fairly sophisticated and that the targets for protectionism were Russia and China. His concern was that any legislation would cause collateral damage.

¶11. (SBU) Saeed stressed that guidelines would allow ADIA to distinguish itself from other SWFs. Al-Otaiba noted that SWF guidelines seemed like a good preemptive measure and that working with the IMF would remove the perception that this was a US-imposed solution. He said that he thought Abu Dhabi's investment organizations would be helpful as long as they did not feel "singled out or pressured" and as long as the guidelines were not too intrusive. He explained that he would be visiting Washington late September/early October to discuss the UAE arms package and said that he would raise the issue of SWF with his congressional interlocutors, if necessary.

Comment

¶12. (SBU) All Abu Dhabi interlocutors welcomed the opportunity to cooperate with the USG. Both Sheikh Ahmed and Al-Otaiba responded positively to the proposal for voluntary best practices although Sheikh Ahmed stressed that he would want to see further details. Al-Otaiba even welcomed the idea of working through the IMF/WB since it would minimize the impression that this initiative was being forced on SWFs by any one country. Al-Kindi was too focused on ADIC's portfolio management responsibilities to be able to focus on a bigger political picture although, as a government employee, he is not likely to oppose an Abu Dhabi government decision. One sticking point for Abu Dhabi on the question of SWF guidelines could be the degree of transparency that is sought. Sheikh Ahmed and Al-Suwaidi stressed that ADIA did not want to keep secrets from governments in recipient countries, but strongly expressed their discomfort with the idea of raising ADIA's public profile or speaking to the press. Post will continue to follow up with ADIA, ADIC, Mubadala, and the Emirate of Abu Dhabi government. End

Comment.

¶13. (U) This cable was cleared by DAS Saeed's party.
SISON